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IN THIS ISSUE:

Japan's Current Account Surplus Continues To Increase Despite Decline In Export Volume 1

Yen Approaches Y150=$1.00 Level 4

Gorbachev Underscores Asian Ties 5

Gray Market Legislation Proposed 6

Baldrige To Japan: "Act Now!" 7

Questions Mute U.S. Industry Reaction To Semiconductor Pact 8

Notes 10

Japan's Current Account Surplus Continues To Increase Despite Decline In Export Volume

Capped by a $7.6 billion surplus in June, Japan's current account balance -- which includes trade, services and transfers -- hit a record $35.9 billion in the first half of 1986, compared to $20.1 billion during the same period of 1985 (see Table 1). It therefore appears likely that the surplus for 1986 will reach the $77 billion mark predicted by the Organization for Economic Cooperation and Development. It is equally probable that trade on a balance of payments basis will come close to the OECD's projection of an $84.8 billion surplus since, in just the January-June period, exports exceeded imports by $38.4 billion, up from $23.1 billion in 1985's first six months.

The rising current surplus reflects a reduction in the services deficit in addition to the expanding trade surplus. The services deficit in the first

half of 1986 was $1.3 billion, compared to $2.2 billion during the same period of 1985; the June deficit was just $20 million. In particular, net income from overseas investments continues to rise, reflecting Japan's position as the largest net creditor nation.

Table 1: Japan's Balance of Payments

(in millions of dollars)

	Trade Balance	Exports (f.o.b.)	Imports (f.o.b.)	Services (net)	Current Account Balance	Long-Term Capital (net)
1981	$19,967	$149,522	$129,555	$-13,573	$4,770	$-9,672
1982	18,079	137,663	119,584	-9,848	6,850	-14,969
1983	31,454	145,468	114,014	-9,106	20,799	-17,700
1984	44,257	168,290	124,033	-7,747	35,003	-49,651
1985	55,986	174,015	118,029	-5,165	49,169	-64,542
1985:I	8,937	38,164	29,227	-1,565	6,818	-10,355
1985:II	14,193	43,239	29,046	-611	13,262	-17,166
1985:III	15,077	43,469	28,392	-1,641	13,095	-18,309
1985:IV	17,779	49,143	31,364	-1,348	15,994	-18,712
1986:I	14,593	45,089	30,496	-1,163	12,718	-18,950
1986:II(p)	23,765	52,247	28,482	-150	23,158	-29,149

Source: Bank of Japan

Japan's continuing record surpluses have given rise to increasing doubts about the effectiveness of exchange rate changes in reducing trade imbalances. A study by World Economic Information Services, which assumes an exchange rate of Y168=$1.00, predicts that Japan's total trade surplus on a payments basis in 1988 will reach $96.7 billion (compared to $56 billion last year). The Bank of Japan's latest quarterly report called for expansion of domestic demand and structural changes, including tax reform, business deregulation and urban redevelopment, to increase imports. Bank of Japan governor Satoshi Sumita, who views the external trade imbalance as the largest issue facing Japan's economy, has stressed that exchange rate realignments alone can have only a limited effect on the trade imbalance.

Changes in the volume of trade, however, show that the sharp appreciation of the yen since September is having the desired effect on trade flows. Compared to year-earlier levels, export volume fell for the fourth consecutive month in June (down 2.3 percent), while import volume rose for the tenth consecutive month. Eventually these volume changes should reduce the dollar value of Japan's trade surplus. Economists estimate that it takes 6 to 18 months for currency changes to reduce trade imbalances.

On a customs clearance basis, the dollar value of Japanese exports rose 20 percent during the first half of 1986 from the year-earlier level, while imports fell slightly, doubling the trade surplus to $34.2 billion (see

Table 2). The surplus with the United States was $23.1 billion (compared to $16.8 billion in the first half of 1985), while the surplus with the European Community was $8.3 billion (compared to $4.8 billion). Lower oil prices cut Japan's deficit with the Middle East to $5.9 billion in the first half of 1986, compared to $9.6 billion during the same period a year earlier.

Table 2: Japan's Exports and Imports in Dollar Terms

(in millions of dollars)

Year	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1981	$152,030	17.1%	$143,290	2.0%	$8,741
1982	138,831	-8.7	131,931	-7.9	6,900
1983	146,928	5.8	126,393	-4.2	20,534
1984	170,114	15.8	136,503	8.0	33,611
1985	175,638	3.2	129,539	-5.1	46,099
1985:I	38,503	-1.3	32,513	-5.7	5,990
1985:II	43,748	0.6	32,094	-7.0	11,654
1985:III	43,909	2.7	31,239	-8.0	12,671
1985:IV	49,478	10.3	33,693	0.5	15,784
1986:I	45,520	18.2	33,060	1.7	12,460
1986:II(p)	53,154	21.5	31,447	-2.0	21,707

Source: Japan Tariff Association

Table 3: Japan's Exports and Imports in Yen Terms

(in billions of yen)

Year	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1981	Y33,469	13.9%	Y31,464	-1.7%	Y2,005
1982	34,433	2.9	32,656	3.8	1,776
1983*	34,909	1.4	30,015	-8.1	4,895
1984	40,325	15.5	32,321	7.7	8,004
1985	41,956	4.0	31,085	-3.8	10,871
1985:I	9,898	9.5	8,340	4.3	1,559
1985:II	11,025	11.0	8,093	2.8	2,932
1985:III	10,591	2.4	7,534	-8.2	3,057
1985:IV	10,442	-5.3	7,118	-13.5	3,324
1986:I	8,678	-12.3	6,345	-23.9	2,333
1986:II(p)	9,117	-17.3	5,403	-33.2	3,714

Source: Japan Tariff Association

The yen value of Japanese exports fell 15 percent in the first six months of 1986, but the trade surplus continued to rise as a result of a 28.5 percent contraction in imports (see Table 3). Declining purchases from Middle East countries accounted for more than one-third of this drop. The surplus with the United States, though, fell in yen terms, reflecting an 11.6 percent decline in shipments to this country.

Randall S. Jones

Yen Approaches Y150=$1.00 Level

Continued pessimism about the outlook for the U.S. economy helped the yen soar to new heights last week, reaching a postwar record of Y152.8=$1.00 August 4. The latest surge left the yen 58 percent above its level prior to the September 22, 1985 five-nation agreement to lower the value of the dollar.

Most analysts blame the decline in the dollar on the steady stream of negative economic reports coming out of Washington, leaving foreign investors and central banks disenchanted with holding dollars. Recent indicators do not point to an acceleration of the 2.4 percent real economic growth rate registered in the first half of the year. News that the June trade figures showed the U.S. trade deficit running at $170 billion annually also reduced confidence in the dollar. Another factor was the July 30 speech by Secretary of State George Shultz, who suggested that the Reagan administration expects further declines in the U.S. currency.

Finance Minister Kiichi Miyazawa, who believes the yen should return to the Y160 to Y170 range, announced his ministry is considering relaxing the remaining controls on capital outflows. Increased overseas investment would strengthen the dollar by promoting the sale of yen for dollars. Long-term capital outflows in the first six months of 1986 totaled $48.1 billion compared to $27.5 billion during the same period of 1985.

One specific proposal being considered by MOF is an increase in the limit on purchases of foreign bonds and other securities by insurance companies and trust banks. This proposal is typical of the financial liberalization pattern of the past 10 years; restrictions on capital inflows are lowered during periods of a weak yen and outflows are encouraged when the yen rises.

Bank of Japan governor Satoshi Sumita agreed that the relaxation of controls on capital outflows would be an effective way to slow the yen's appreciation. Although large-scale intervention, estimated at $1 billion on August 4 alone, has failed to stabilize the yen, Mr. Sumita said that the central bank will continue to intervene in exchange markets. Despite the strength of the yen, the central bank governor said that he has no plans to further lower the official discount rate. Three cuts already this year have reduced it to the historically low level of 3.5 percent. Mr. Sumita said that surging land and stock prices are partly a result of relaxed credit conditions and require close monitoring.

Randall S. Jones